No. 5493.

IN THE

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

Lewis N. Merritt,
Appellant,

vs.

S. H. Peters,
Appellee.

APPELLEE'S BRIEF.

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We regret at the outset of this brief, the necessity of correcting one of the vital portions of the statement of facts made by counsel for the appellant, a misstatement which we believe misled the Special Master on the argument before him and which caused him to make incorrect findings on the question of whether or not the bankrupt had the automobiles in his possession, and the correction of which caused the district judge to reverse the findings of the referee as being contrary to the evidence and to deny the bankrupt his discharge. There is no dispute of the fact that Lewis N. Merritt was adjudged a bankrupt on April 1, 1927, nor do we dispute the statement of counsel regarding the pictures left the bankrupt and his brother and sisters under the terms of the will

of Annette W. Merritt. Neither do we dispute the fact that the bankrupt was purchasing these automobiles during a period of approximately six months before bankruptcy, purchase being made under conditional sales contract.

We do, however, dispute the statement at the bottom of page 4 and top of page 5 of appellant's brief, "At the time the schedules were sworn to and filed, the automobiles were not in the possession of appellant," citing record, pages 30 and 47, for the reason that the bankrupt himself admitted that at the time that he verified these schedules in bankruptcy, he did not doubt for a moment but that he had these automobiles in his possession. [Record, page 52, beginning at line 17.]

The statement of counsel on page 5 of his brief that "Schedule A2 was amended under date of May 3, 1927," citing the record on page 36, is misleading to say the least. The record shows that the amendment to the bankrupt's schedules was not made on May 3, 1927, as stated by counsel, but was made on or subsequent to May 24, 1927, and if counsel saw fit to date his amendment back it is no concern of ours and in no way binding upon us. We refer the court to page 40 of the record wherein Mr. Hacker offers in evidence transcript of the proceedings of May 24, 1927, wherein he reads in evidence a portion of the transcript of the proceedings as Objecting Creditor's Exhibit No. 1, to show that on May 24, 1927, or later he amended the schedules. We therefore ask the court to take into consideration these two corrections which we deem vital, particularly the first one, relating to the possession of the automobiles at the time of filing of the petition in bankruptcy.

ARGUMENT.

We consider appellant's first point as being wholly without merit. Conditional sales contracts, like all other contracts, are made subject to the laws of the state and the laws of the United States, including the Bankruptcy Act. Section 47-A of the Bankruptcy Act reads in part as follows:

> "And such trustees, as to all property in the custody or coming into the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies, and powers of a creditor holding a lien by legal or equitable proceedings thereon; and also, as to all property not in the custody of the bankruptcy court, shall be deemed vested with all the rights, remedies, and powers of a judgment creditor holding an execution duly returned unsatisfied."

Section 689-A of the Code of Civil Procedure of the state of California reads as follows:

> "Personal property in possession of the buyer under an executory agreement for its sale entered into after this section goes into effect may be taken under attachment or execution issued at the suit of a creditor of the buyer, notwithstanding any provision in the agreement for forfeiture in case of levy or change of possession." (New section added May 25, 1921; Stats. 1921. P. 391.)

Therefore under the provisions of section 47-A of the Bankruptcy Act and 689-A of the California Code combined, the provision in the conditional sales contract providing for forfeiture in the event of levy was an absolute nullity.

Appellant's second point falls of its own weight. By appellant's own statement of the fact, he concedes that

the Packard car was worth $1100.00 on April 1, 1927, with a balance due of $1016.76, leaving an equity of over $80.00 in the Packard. He also concedes that the trustee realized $900.00 on the two automobiles when he sold them, and it is no concern of ours that the bankrupt may have expended other money on the automobiles after he had attempted to conceal them from his trustee.

Arriving at point three of appellant's brief, we believe this to be the crux of the entire situation. The bankrupt took the witness stand as a witness in his own defense. On cross-examination he admitted remembering Mr. Lewis (attorney for one of the creditors) examining him in court relative to these automobiles on May 24th. He admitted that Mr. Lewis asked him if he had any automobiles and the kind of a car that it was, and that he answered. "Yes, and that he had paid about $3200.00 for it." [Record, page 50.] He admitted on cross-examination "that Mr. Lewis asked him if he was driving that car and that he said that he was and that he meant just what he said when he made that statement." [Record, page 51.] Further down on the same page we find his memory being further refreshed when he was asked if Mr. Lewis did not ask him the following questions:

"Q. Have you got it with you today?

A. No.

Q. Where is it?

A. In Pasadena.

'Q. What did you mean by that?

A. I suppose I meant it was in Pasadena instead of being here.

Q. Is it not a fact that car was repossessed two days after that examination?

A. I delivered the car rather than have the notoriety and publicity'." [Record, page 51.]

On page 52 of the record we find the amendment to the settled record relating to the bankrupt's admission that he had these automobiles in his possession at the time of the drawing of the original schedules in bankruptcy. In order that there may be no misapprehension as to the true facts regarding this admission, we shall set out for the court the questions and answers from the original reporter's transcript, the original record as prepared by counsel for the appellant and the amendment as asked for by appellee. The original reporter's transcript of the testimony reads as follows:

> "Q. It is a fact that at the time you drew the original schedules in bankruptcy and particularly that part relating to horses, carriages and other vehicles, that you had both of these automobiles in your possession?
>
> A. I don't doubt but that I did have them."

In settling the record, counsel for the bankrupt attempted to put this question and answer as follows:

> "At the time the original schedules were drawn I don't doubt that I had them in my possession."

The amendment proposed by counsel for the appellee read as follows:

> "On the same page (29), commencing at line 6, of the appellant's statement of evidence, correct to read:—
>
> At the time the original schedules were drawn, I don't doubt that I had these automobiles in my possession." [Transcript, page 105.]

This amendment was not allowed by the District Court, as we contend should have been done. If this court de-

sires it, or if counsel disputes the fact that the word "them" refers to automobiles, and not to schedules, we believe that the original reporter's transcript should be certified up in order that no dispute as to the significance of this vital admission may arise and no misunderstanding result therefrom.

The necessity for this amendment and the wisdom of it is patent on its face. The statement as made by counsel for the appellant standing alone, could very easily be construed to mean that at the time of drawing up the original schedules in bankruptcy, the bankrupt had the *schedules* in his possession, which would place an entirely different meaning on the damaging admission made by the bankrupt that at the time the schedules were drawn, he did not doubt but that he had these automobiles in his possession. Further down on page 52 of the record, we find the following:

> "Q. What did you mean by your answer on page 7 under date of May 24, 1927, when you were asked the question:
>
> 'Q. Are you driving that car?
>
> A. I am.'
>
> Q. What did you mean by your answer to that question?
>
> A. What date was that?
>
> Q. May 24, 1927, the second meeting here.
>
> A. If I could get the record, I could tell and I don't see why the Commercial Discount Company don't have it, because it would show exactly.
>
> Q. Here is the transcript of your answer as to that on May 24, 1927, and you knew at that time, the time you gave that testimony, whether or not you had possession of that car.
>
> A. I presume I did.

Q. What did you mean by saying that you were driving that car at that time, May 24, 1927?

A. I don't know. I don't know—I don't remember what I testified.

Q. As a matter of fact that car was in your garage at Pasadena on that date?

A. I don't know. I can't tell.

Q. What did you mean when you said it was in Pasadena?

A. I meant it was in Pasadena.

Q. Whereabouts in Pasadena?

A. I don't know.

Q. What did you mean by answering that question that way?

'Q. What other automobiles have you?

A. I have a Nash roadster my son uses.

Q. A Nash that your son uses?

A. Yes.

Q. Where did you get that?

A. I bought that from Earl C. Lindley.'

Q. Did you remember that testimony?

A. Yes."

We ask the court to note that in referring to the Nash roadster Mr. Merritt on May 24, 1927, over a month and a half after filing his petition and his adjudication in bankruptcy, says that he "has a Nash roadster that his son uses." It is significant that he refers to this Nash roadster in the present tense and not in the past tense.

On page 56 of the record counsel for the objector endeavored to get an explanation out of Mr. Merritt as to what he meant by his answer "I have a Nash roadster my son uses" and brings forth the lame explanation:

"A. I meant I had bought it for the use of my son.

Q. And your son used it at that time?

A. I don't know that, I couldn't tell you unless—and there must be some record that somebody can get that will show the exact dates those cars were in my possession and the exact dates that they were not in my possession."

The significant admission made by the bankrupt on page 57 would indicate that the alleged repossessions were only technical. The bankrupt on cross-examination stated as follows:

"A. I cannot tell when was the first time that I returned these automobiles to Earl C. Lindley. I know they were there four different times. The first time was before the first of April, 1927, and the cars were left there for several weeks. I cannot recall the date of the second time. Mr. McDonald asked me to leave the cars there until the payments were made up.

Q. Then at the time you turned these cars back to Mr. Lindley's garage, they were turned back with the understanding with the finance company that was holding the contract, that they would be left there until the payments were made up?

A. That was the way they talked to me." [Record, page 57.]

In the middle of page 58, we learn that this was not the first experience this bankrupt had had in the bankruptcy courts. A corporation in which he owned fifty per cent of the stock had gone into bankruptcy some years before. The bankrupt was an officer of the corporation and had been examined in the bankruptcy court in connection with that corporation's failure and that he knew it was the duty of a bankrupt to schedule all of

his assets, is admitted. On page 59 he evades the answer to the pointed question:

> "Q. And you knew at that time you verified these schedules that you had an investment of $2000.00 in these automobiles, did you not?
>
> A. I considered that with Mr. Morris and it was talked over as to the equity in it, or in them."

In connection with the strenuous contention of appellant and the finding of the Special Master:

> "That shortly prior to the bankruptcy the payments were delinquent and the cars were repossessed by the legal owner thereof" [Record, page 12],

the testimony is extremely vague and uncertain. A careful examination of the testimony of the three witnesses, who would know the facts, to wit: Earl C. Lindley, president of the Earl C. Lindley Motor Company, who sold the cars to Mr. Merritt, Frank McDonald, adjuster for the Commercial Discount Company, the finance company that purchased the contracts from Mr. Lindley, and Lewis N. Merritt, the bankrupt himself, would indicate that the first repossession of these automobiles took place on March 18, 1927, at which time the Commercial Discount Company had at least one of the automobiles in the Earl C. Lindley Motor Company's place of business for a period of approximately two weeks. [Testimony of Frank McDonald, record, page 61.] Of this alleged repossession, Mr. Lindley does not testify. It is significant to note that Mr. McDonald testifies that they "had the car in the Earl Lindley Motor Company's place of business about two weeks when we released it," and that the March payment was made which brought it down to April 5, 1927. Now this alleged repossession is easily

capable of mathematical calculation and reason. March 18, 1927, was on a Friday. Assuming that the car was kept exactly two weeks, it was then released to Mr. Merritt on April 1, 1927, *the very day of his adjudication in bankruptcy.* Certainly, reason would dictate that it was released prior to April 5, 1927, for no finance company that had been compelled to repossess one or more automobiles from a purchaser for nonpayment of his installments would release the car or cars back to him without being paid at least up to date. This, coupled with the bankrupt's admission that he "did not doubt that at the time of executing his schedules in bankruptcy, he had both of these automobiles in his possession" is especially significant, and leads to the reasonable conclusion that the Master was confused by the sleight of hand performance indulged in with regard to the possession of these automobiles by the Commercial Discount Company, the Earl Lindley Motor Company and the bankrupt.

The second repossession took place on April 18, 1927, as testified to by the witness McDonald on page 61 of the record. He says:

> "The second time we took it back was on April 18th. The April payment was then behind. The car was worth at that time $975.00 or $1000.00." [Record, page 61.]

The third "repossession" took place on May 26th, 1927. The witness McDonald testifies:

> "And the other time we took it back was on the 26th day of May. When we took it back in April we retained it approximately three or four weeks. I told Mr. Merritt that we were going to hold it for a reasonable length of time." [Record, page 61.]

It is especially significant that this repossession on the 26th day of May occurred two days after the disastrous examination held before the referee on May 24, 1927, at which the bankrupt testified that he did not have any automobiles and that the automobiles that he had been buying on sales contract were in the hands of Earl C. Lindley Motor Company. [Record, pages 24-25.]

The final repossession of these cars occurred on October 13, 1927, as testified to by the witness Earl C. Lindley. He says:

> "They came back into the possession of the Earl Lindley Motor Company on the 13th of October." [Testimony of Earl C. Lindley, record, page 23.]

Turning then to the trustee's petition for a turn over order and the order to show cause issued by Referee Earl E. Moss, at that time in charge of these proceedings, it is particularly significant to note that the bankrupt was required to show cause on the 14th day of October, 1927, at the hour of ten o'clock A. M., why an order should not be entered requiring him to turn over these two automobiles to his trustee. [Record, page 29.] Service of this order to show cause was admitted by N. W. Hacker and H. M. Tichner, attorneys for the bankrupt, on October 8, 1927. It is especially significant to note that these cars were again "repossessed" the day before the hearing on the turn over order before Referee Moss. Whether the bankrupt turned them back or whether the finance company's representative came and got them is immaterial. Tracing these cars and their possession is almost as bewildering as the old "shell game" at the county fairs of years gone by when the farmer was

asked to tell under which shell the little pea could be found. First they were with the bankrupt, then the dealer, then the finance company, then the bankrupt again and so on *ad infinitum*. In any event, whenever it suited the bankrupt's purpose, or his son's purpose, to use these cars, the dealer and the finance company seemed to have been strangely considerate and willing to return them, and when brought into court on any proceeding concerning them, they were always out of the bankrupt's hands, from the day of the first examination down to the time that he was compelled by order of the court to execute a transfer of them to the trustee. Taking into consideration the fact that this case was handled by two different referees, James L. Irwin, Esquire, the original referee in charge of the proceedings before whom the first examination was conducted and who finally passed on the application for discharge as Special Master, and Earl E. Moss, Esquire, the other referee in bankruptcy in Los Angeles, who handled the proceedings for turn over order, during the absence of Referee Irwin from the district, and further taking into consideration the lightning changes of possession of these cars by the various parties concerned, it is small wonder that error crept in in the Master's findings on discharge.

Insofar as the bankrupt's testimony is concerned, it is so vague and indefinite that were it not for his admission "that he did not doubt for a moment that at the time of filing his schedules in bankruptcy he had them in his possession" his testimony would be of no value whatsoever. On page 46 of the record he says:

> "I had delivered the cars on four different occasions at the request of Mr. McDonald because I

could not make the payments when they became due and I would deliver them to Lindley and leave them there until I could make the payments and I can't state, unless I can find the records showing those payments, what the dates were, and when I did get the money, I would go and pay up on the cars and take them and use them and that it not only happened once, but it happened four times; but only twice I think did they serve papers on me.

"Q. Were you contemplating filing a petition in bankruptcy when you delivered them the last time?

A. No, sir.

Q. And you can't approximate the length of time prior to the filing of your petition here, it was you delivered the cars?

A. No, sir.

Q. Whether it was the day before, a week before, a month before, or how long?

A. No, I couldn't. I wish I could find some records, but I have none myself. I tried to look over Mr. McDonald's records to see when I made the back payments, that would be the only way I would know." [Record, page 46.]

On page 48 we find the following:

"Q. How did you know he still had possession of them when you went after them the second time. Did you go to him in the meantime?

A. Mr. McDonald came to collect on them just the same whether I had the cars or not." [Record, page 48.]

The bankrupt here attempts to mislead the court into believing that the finance company could collect the payments even though they had repossessed the cars. Such a contention is absolutely foolish. Mr. Merritt was in

bankruptcy and his provable debts were in line to be discharged, regardless of whether they were for automobiles or anything else. Mr. Merritt knew this or he would not have gone into bankruptcy. And for him now to seek to contend that his reason for taking the cars back was that the finance company was still collecting installments after he had gone into bankruptcy and after they had repossessed the cars, is too ridiculous for further argument. It is our contention, and we believe it was the opinion of the learned district judge, that when Mr. Merritt went back to the Earl C. Lindley Motor Company in June, 1927, and paid up the April 5th and May 5th installments on his cars, he knew that the cars had "been held for a reasonable length of time" as Mr. McDonald testified. [Page 61.] His bankruptcy was in the hands of able and learned counsel and in view of the fact that he seems to have seen fit, according to his own admission, to have scrupulously consulted an attorney regarding omitting these cars from his schedules, it seems peculiar to us that he did not consult his counsel regarding an automobile finance company trying to collect installments from him on two cars which had been taken away from him and which were even then in their hands. If the situation were as Mr. Merritt would have us believe, his counsel would no doubt have assured him that the filing of his petition in bankruptcy had relieved him from liability for any deficiency under the conditional sales contracts which he had signed regardless of how favorable they might be to the finance company.

We believe that the Fourth and Fifth points urged by counsel may be consolidated under the question of whether or not the bankrupt acted in good faith and on

advice of counsel. We frankly admit that if the bankrupt acted in good faith and on advice of counsel, his discharge should not be denied, but we also contend that the burden was on him to prove good faith and advice of counsel even prior to the amendment of 1926, under which this case was handled. Section 14 B 7 reads in part as follows:

> "Provided, that if, upon the hearing of an objection to a discharge, the objector shall show to the satisfaction of the court that there are reasonable grounds for believing that the bankrupt has committed any of the acts which, under this paragraph (b), would prevent his discharge in bankruptcy, then the burden of proving that he has not committed any of such acts shall be upon the bankrupt."

The objecting creditor had built up his case by proving the following facts:

First: That the bankrupt had filed his schedules on March 31, 1927, and had sworn to Schedule B2g of said schedules as follows:

> "Carriages and other vehicles, viz.: None."

[Specification of Objection No. 2, record, page 7, and testimony of Clara E. Larison, notary public, record, page 20], and that at the time of swearing to said schedules, the bankrupt had two automobiles, a Packard and a Nash, in his possession, which automobiles he was purchasing on conditional sales contract [Record, page 52].

Second: That at the time of his first examination in the referee's court on May 24th, he came down town in a car and on his examination was asked by Mr. Lewis:

"Q. Have you any automobiles?
A. No."

And further down at the bottom of page 24 of the record we find him admitting that on that date, May 24, 1927, he was driving the Packard car which he had purchased for $3200.00 and on which he had paid $1600.00. These two facts alone, the omission of these automobiles from his schedules and his undisputed possession of them on the date of his examination, indicate without question the commission of three offenses under section 29B of the Bankruptcy Act, concealment of the automobiles from his trustee, false swearing in his schedules and false swearing on his examination, when he swore that he had no automobiles. A complete case was established against him, and, standing undisputed, these facts should serve to convict him beyond all reasonable doubt. The burden then shifted to him and he advanced the defense that he had acted in good faith and on advice of counsel.

It is well established that in order to maintain the defense of advice of counsel it is necessary that the person seeking to establish this defense show that he made a full, fair and complete disclosure to his counsel of all of the facts on which he sought the advice. What did the bankrupt show? Nothing whatsoever except a naked, unsupported statement by himself that his attorney advised him to leave these automobiles out of his schedules. He says at page 52 of the record:

> "At the time I verified these schedules I had a conversation with my attorney relative to the automobiles. I do not remember just what I said to him. He said that I had no equity in them and that they did not belong to me. I do not know that my de-

fense is that I made a full and fair disclosure to my attorney. I don't remember what he said. He simply said that they didn't belong to me, that I had no right to schedule them. I told him that I wanted to turn in everything I had and that I had these on sales contracts. I did not tell him where they were. When we drew up the schedules I didn't know myself where they were. I told him the truth about them and I don't know now at that date what it was." [Record, page 52.]

On page 58, we find the following:

"Q. You knew, however, that it was the duty of a bankrupt, did you not, to schedule all of his assets?

A. Yes. I had that common knowledge. I know it is the duty of the bankrupt to schedule all of his assets.

Q. And you knew, at the time you verified these schedules that you had an investment of $2000.00 in these automobiles, did you not?

A. I considered that with Mr. Morris and it was talked over as to the equity in it, or in them.

Q. Did you not testify here yesterday that you did not remember what conversation you had with Mr. Morris and that you could not tell the court what you told Mr. Morris and what Mr. Morris told you?

A. I told you I couldn't tell what I—what we talked about, my recollection is that he advised me that he had—that that was the way to handle it.

Q. As a matter of fact you were worried enough about the cars to consult your attorney about them?

A. Well, Mr. Morris and I went through everything.

Q. It was not a case on your part of forgetting the cars; that was not the reason why they were not listed; you knew you had them.

A. I couldn't tell, because in the contracts it said I had no rights and that they were not my property and I was at a loss about them and I simply left it up to my attorney.

Q. But you don't remember what you told your attorney?

A. I don't remember the exact conversation, no." [Record, pages 58-59.]

The above, when coupled with the bankrupt's version of the alleged consultation at page 52, and his damaging admission following, disposes of this defense.

> "The schedules were amended subsequently on the advice of Mr. Hacker. At the time the original schedules were drawn, I don't doubt that I had them in my possession." (Referring to the automobiles) (Parentheses ours.) [Record, page 52.]

> "Advice of counsel, if asked for and acted on bona fide, is valid evidence to negative fraudulent intent and knowledge on the bankrupt's part in omitting assets from schedules, or otherwise not revealing them.
>
> But advice of counsel will not excuse an omission of assets from the schedules where there were no substantial legal questions involved and the actual legal relation of the property to the bankrupt's estate was matter of common knowledge and plain to everybody. Nor will it excuse where the facts were not fully laid before counsel." (Remington on Bankruptcy, Vol. 7, sections 3243-3244.)
>
> Renmers v. Merchants Leclead National Bank, 173 Fed. 484, 23 A. B. R. 78. C. C. A., Missouri.

In the matter of Breitling, 133 Fed. 146, 13 A. B. R. 126, we find a situation almost parallel with the instant

case. In the Breitling case the bankrupt omitted from his schedules an order from the Waldheim Cemetery Company for $40.00 worth of lumber given shortly before bankruptcy. At the time he filed his petition he was ignorant of the fact as to whether the lumber had been delivered from his yard to the company or not. The district judge found that he had conferred with his counsel, Messrs. Guthrie and Palmer, concerning this matter and that he was ignorant of the fact that the lumber was still in his possession and, acting under their advice, he did not schedule it. Two days after he filed his petition in bankruptcy he collected the amount paid for the lumber and applied it on costs and attorney fees and the district judge held that the bankrupt was relieved of fraudulent intent for the reason that he had acted on advice of counsel. The District Court found that his attorneys had advised him that he was entitled to this money, inasmuch as he had been entitled to exemptions of $400.00 anyway, and granted the discharge. On appeal the United States Circuit Court of Appeals for the 7th Circuit said:

> "The Act required the fullest disclosure the utmost good faith, the surrender of all his estate not exempt under the Act. It is well observed by Judge Brown that: 'A discharge in bankruptcy upon any other condition than the complete appropriation of every known asset legally available to the creditors, would not only be a glaring wrong to creditors, but contrary to every conception of a just system of bankruptcy.' (*In Re* Beaudoine, 96 Fed. 536-539, 3 A. B. R. 55.) If it be doubtful whether a specified item of property should go to creditors or be reserved by the bankrupt, it is not for him to constitute himself the judge, concealing the fact, but it is his duty

to disclose the transaction, that the bankruptcy court may determine the right. (*In Re* Gaily, 127 Fed. 538, 11 A. B. R. 539.)

"Without question the claim against the Waldheim Cemetery Company should have been scheduled. This the referee concedes in his report. It was knowingly and designedly omitted by the bankrupt. This is conceded by him. But he insists it was so done upon the advice of counsel. But advice of counsel cannot excuse violation of law. It may mitigate the act according to the character of the advice and circumstances under which it is given. If the omission here were in the exercise of a supposed right under advice taken and given in good faith, the bankrupt might be absolved of the charge of making a false oath or of designedly concealing his estate from his creditors. To work such result, however, the facts must be fully and in good faith stated to counsel and the act charged done innocently and believing that he had been correctly advised."

Further down in the same opinion in the last paragraph the court says:

"This question of fact rests upon the statement of the bankrupt. It does not satisfactorily appear that he fairly presented the case to his counsel, or that his counsel advised him that he was entitled to retain the account as exempt, in addition to the $400.00 of exemptions claimed, or that he could properly omit it from the schedules. We should be loathe to believe that counsel could so have advised him and he has not called upon them to verify his statement, weak and inconclusive as it appears. The facts here, which are fully established lead us to the conclusion that the bankrupt purposely retained and concealed from his creditors that to which he was

not entitled and knowingly made false oath to his schedules. The amount involved, it is true, is small, but the design to conceal was deliberate and is clear. We are indisposed to give countenance in the slightest degree to any act which shall withhold from creditors any part of the estate of a bankrupt which lawfully he should devote to the payment of his debts.

The decree is reversed." (*In Re* Breitling, 133 Fed. 146, 13 A. B. R. 126, C. C. A., Illinois.)

In the courts of California, we find the rule requiring full, fair and honest disclosure of the facts to be the same.

"The defendant, in malicious prosecution, cannot maintain the existence of probable cause in law by proving that he acted upon the advice of counsel, unless he shows that he made to such counsel before receiving the advice, a full, fair and honest statement of the facts then known to him bearing upon the guilt of the accused person." Stone v. Wolfe, 168 Cal. 261, citing Dawson v. Schloss, 93 Cal. 202, 29 Pac. 31; Dunlap v. New Zealand, etc. Co., 109 Cal. 371, 42 Pac. 29; Bliss v. Wyman, 7 Cal. 257; Wild v. Odell, 56 Cal. 136. Also see Burke v. Watts, 188 Cal. 119.

In Auner v. Norman, 29 Cal. App. 425, the defendant testified:

"I disclosed to him (Conkey) fairly and truthfully all of the facts that were within my knowledge concerning the matter of the charge against Mr. Auner at that time and before filing the criminal complaint."

This statement the District Court of Appeal for the Second Appellate District of the State of California held

insufficient to justify the defense. There are dozens of other authorities holding the same way, but we believe it unnecessary to cite any more decisions. As to the case of *In Re* Breitling, 133 Fed. 146, 12 A. B. R. 126, one could search the records through and we do not believe it would be possible to find a case more closely in point throughout. In the Breitling case the bankrupt did not know whether or not he had the lumber in his possession at the time of filing his schedules. In the instant case Mr. Merritt claimed he did not know where the automobiles were at the time of filing his schedules. In the Breitling case, Mr. Breitling consulted his attorney and claims he was advised to omit the lumber from the schedules. Mr. Merritt says the same thing regarding the automobiles. In the Breitling case, two days after bankruptcy the bankrupt collected $40.00 from the cemetery company and applied it on his attorney fees and costs. In the Merritt case, Mr. Merritt applied the $2105.55 that he had in these automobiles, prior to the filing of the petition in bankruptcy, on the alleged "repurchase" price when he went to the Lindley Motor Company in June, two months after filing his petition in bankruptcy, paid up the installments that were due on April 5th and May 5th, and converted them to his own use and benefit. In the Brietling case, the bankrupt was unable to tell anything about the conversation had between himself and his attorney, except that the attorney advised him "that he was justified in making that sale and not putting it in." In the Merritt case the bankrupt cannot remember what he told his attorney or what his attorney told him, except that he was buying some cars on conditional sales contract and that his attorney told

him he need not schedule them. In the Breitling case the defense of counsel was advanced on the naked, unsupported testimony of the bankrupt. In the Merritt case we have a similar situation. The bankrupt in the proceeding in the District Court was represented by attorneys Nicholas W. Hacker and Harry M. Ticknor. In this court he is represented by Mr. Hacker alone. Nowhere in the record does Mr. Morris' name appear as an attorney. He was not called as a witness on behalf of the bankrupt, so his testimony is conspicuous by its absence. He was not present at the examination of the bankrupt, nor was he present with Mr. Hacker at the trial of the opposition to the discharge. In the Breitling case the Circuit Court of Appeals seemed to think that it was essential that the attorney at least corroborate the fantastic tale told by the bankrupt in order to have it believed. The situation here, we believe, required that in order to sustain the defense, it was the bankrupt's duty to call Mr. Morris and let him tell from the witness stand just what the bankrupt told him regarding the situation and what advice he gave the bankrupt.

For the objecting creditor to attempt to call Mr. Morris would be as unethical as it would be foolish. Communications between Mr. Morris and the bankrupt would be privileged and the objecting creditor would not be permitted to examine him regarding conversation and disclosures made to him in his professional capacity. The bankrupt, however, had a perfect right to call Mr. Morris to corroborate his lame and halting excuse. This he failed to do, although the trial on the opposition continued over two different days. We are confident that Mr. Morris would never have given this bankrupt such

foolish and silly advice if the facts had been disclosed to him truthfully, if in fact he ever really gave the advice. We have only the bankrupt's unsupported version of it and nothing else. It was within the bankrupt's power to fully enlighten the court in this regard and this he failed to do. He should therefore suffer the consequences. (Schmidt v. Union Oil Co., 27 Cal. App. 366.)

It is our contention that in order to sustain the defense of advice of counsel, it was necessary for the bankrupt to prove affirmatively that he had full and fairly stated to his counsel:

(1) That on March 31, 1927, when he was about to file his schedules he had in his possession a Packard sedan, worth $2176.14, on which he had paid a down payment amounting to $651.00 on October 5, 1926, and had made monthly payments of $84.73 thereon on November 5th, December 5th, January 5, 1927, February 5th and March 5th, and that he had a Nash roadster which he had purchased on October 5, 1926, for $2088.84, with a down payment of $624.00 and had made monthly payments of $81.38 each, on November 5th, December 5th, January 5, 1927, February 5th and March 5th, making total payments on both automobiles of $2105.55. He should have further told his counsel that his payments were paid up to six days beyond the date of the verification of these schedules. He should have told him that he was driving one of the automobiles and his son was driving the other. [Record, page 25.] He should have shown the conditional sales contract to his counsel and he should have told his counsel that no installments were then due or past due on said automobiles.

(2) He should have proved on the hearing of the opposition to the discharge that Mr. Morris, with all these facts in his possession, had advised him that his $2100.00 equity in these automobiles was a nullity; that he was not required to schedule it as an asset and that he had a right to keep and retain these automobiles without disclosing his equity to the trustee.

As to his failure to prove these essential facts, the record speaks for itself. Counsel for the objector was more than fair in this respect in giving the bankrupt an opportunity which his own attorney had overlooked, to fully and fairly disclose to the court on cross-examination what he had told Mr. Morris. But, notwithstanding the effort of counsel for objecting creditor to bring out the conversation, for some reason or other the bankrupt did not see fit to disclose it. This defense therefore, we contend, falls of its own weight.

The Bankrupt Had an Equity in These Automobiles and the Trustee Was Entitled to Any Equity Which the Bankrupt Might Have Had Therein, Regardless of the Fact That the Contracts Provided for Retention of the Title by the Vendor.

It is true that the bankrupt did not have the legal title to these automobiles. He did however have the registered title to both cars under the Motor Vehicle Act of the State of California, and he had also an equitable title to the extent of paid installments. This equity passed to the trustee and the trustee had a right to salvage the equity for the benefit of the general creditors by paying the balance due on the automobiles and selling them for the benefit of the bankrupt estate. Con-

cealment of anything beneficial to the bankrupt, however small the value, constitutes a concealment in bankruptcy and a ground for the denial of a discharge.

> "The offense of fraudulently concealing assets is committed where the bankrupt dishonestly applies money or property to his own use and purposes, so that he himself or some other person whom he may desire to benefit receives advantage and profit by the concealment." (Collier on Bankruptcy, 13th Edition, volume 1, page 899.)

It is true that counsel for appellant contends that the bankrupt's equity in these automobiles at the time of filing his petition in bankruptcy was a nullity. This contention however is refuted by the bankrupt's own subsequent conduct, which argues against him louder than our words. If the bankrupt did not have these cars in his possession at the time of filing his schedules in bankruptcy and the cars had been repossessed two weeks before bankruptcy and were entirely out of his possession, and his rights therein forfeited, as he now seeks to claim, we ask the court to consider why he found it necessary to consult his attorney relative to scheduling them. We also ask the court to consider why, if the bankrupt's equity was of no value whatsoever, he saw fit shortly after the filing of his petition in bankruptcy, to borrow $500.00 from a bank to make the payments which had fallen due on April 5th, five days after his adjudication and May 5th, thirty-five days after his adjudication. The bankrupt had gone into bankruptcy for the purpose of clearing up his indebtedness. Why plunge himself $500.00 into debt, even before his estate was administered, for the purpose of salvaging a worthless equity

in two pleasure cars, if, as he contends, the equity was of no value whatsoever? These automobiles were not repurchased under a new contract. The bankrupt took advantage of the $2100.00 equity which he had in these automobiles at the time of his adjudication and merely resumed his payments, after he thought he had deceived and misled the trustee into believing that the automobiles had been irrevocably forfeited. He did not show where he ever communicated to his trustee in bankruptcy the fact that he had the right and privilege of redeeming these automobiles by making up these back payments. He thereby deceived his trustee and creditors and concealed from them a substantial equity which he deemed it to his advantage to save for his own use and benefit. We refer the court to the record, page 50:

> "Q. I believe you testified on your direct examination that you repurchased these cars from the Earl C. Lindley Motor Company; what was the repurchase price?
>
> A. Well, I said at the time that I did not know whether you would call it a repurchase or not. I went and made a deal with Mr. McDonald on it. Mr. McDonald told me that if I could make payments there would be no objection to my taking the cars. I do not know when that was. There was two months due then."

There is no question but that the trustee had a right to pay up the balance due on these automobiles under General Order No. 28 of the Bankruptcy Act and sections 689A and 689B of Code of Civil Procedure of California, and with this right vested in the trustee the bankrupt was guilty of wilful concealment and perjury throughout the entire proceeding.

Counsel strongly stresses the argument that the bankrupt's effort to file amended schedules and the filing of them and turning over the property to the trustee more than six months after adjudication, when brought in on an order to show cause, tends to purge him of any wrong committed by him. This he cannot do.

> "After he returned from Canada, the bankrupt by leave of the court, filed an amended schedule of assets which included those which he is charged with having concealed, and counsel argues that this related back to his original schedule and operated as an atonement which, being made while the proceedings were yet in progress, redeemed his fault, so that in the end nothing was concealed from the trustee. But we are unable to agree that it would have such an effect. The offenses of false swearing and concealment when once committed could not be retrieved by right and lawful conduct and the doing of things 'meet for repentance,' however they might affect the judgment of the court in imposing sentence." (Kern v. United States, 169 Fed. 617, 22 A. B. R. 223, U. S. C. C. A. 6th Ct.)

CONCLUSION.

We respectfully submit to the court that this is not the usual type of bankruptcy case. We respectfully submit that Lewis N. Merritt is not an unfortunate impecunious debtor burdened down with a load of debts far beyond his ability to pay. On the contrary Mr. Merritt is an unusually fortunate man. Thanks to the foresight of his mother, he is blessed with a spendthrift trust income of $575.00 per month, or approximately $7,000.00 a year from her estate. Contrary to the statement of counsel, the bankrupt is not a man without education or business

experience. The record shows that he is a traveling salesman by profession; that he has been in business before, under the name of Lewis N. Merritt Company, a corporation in which he owned fifty per cent of the stock and was an officer. He was at the time of the trial of the opposition to his discharge acting as guardian of his father. He was not paying any house rent out of his income of $575.00 per month. [Record, pp. 56-57.] There are thousands of hard working honest young men of Mr. Merritt's age in the state of California who would be highly pleased to be able to earn one-third of the income which goes to Mr. Merritt, through no effort of his own, each month. He admits that he knew the duties and obligations of a bankrupt from his experience in putting the Lewis N. Merritt Company through bankruptcy. Seeking now to unload his responsibility for several thousands of dollars worth of personal debts, and to avoid paying these debts out of his princely life income, Mr. Merritt did not even come into the bankruptcy court with clean hands this time and surrender his non-exempt property in order that his creditors might realize the pitifully small dividends that would result therefrom. On the contrary he sought to salvage his equity in these two automobiles and in his desperate attempt to do so, he twice committed perjury. If his equity was worthless, he had nothing to lose by scheduling it in his schedules and giving the trustee an opportunity to abandon it, after due investigation. When unmasked he deceived his trustee and creditors by falsely pretending that the cars had been repossessed and without disclosing to his trustee the fact that such repossession was purely figurative and technical and that he had a right to

vitiate it by paying up the delinquent installments. When driven to the wall with a turn-over order, returnable October 14th, before Referee Moss, he returned the cars the day before the hearing, on October 13th. When the trustee's back was turned. throughout the entire proceeding, Mr. Merritt reclaimed the cars and continued to drive them. The moment the trustee became vigilant or suspicious the cars were always "repossessed." During the alleged "repossession" he does not deny that he was driving the cars. The conclusion that he intended to defraud his creditors is inescapable.

It remains for this court to determine whether a bankrupt purchasing automobiles worth $4200.00 with a substantial equity therein of over $2100.00, can retain his equity as against the trustee in bankruptcy and take advantage of that equity in recovering the automobiles after adjudication. We do not believe that this court will so hold, any more than did the district court. In this day and age with installment sales the rule, rather than the exception, we do not believe this court would be prepared to hold that a contractor, for example, could purchase a fleet of trucks worth say $30,000.00, on contract, pay $25,000.00 of the purchase price, go through bankruptcy, concealing his equity on the grounds that the automobile sales company had reserved the title until all payments were made, and after his adjudication, by borrowing money, pay up the other $5,000.00 and resume operations free from all of his general debts after being granted a discharge.

We have found this bankrupt assuming inconsistent positions throughout, blowing both hot and cold in the same breath. We find him at one time saying that his

equity in these automobiles on April 1, 1927, was of no value whatsoever, and we then find him admitting that he borrowed $500.00 from a bank shortly after his adjudication to pay up the delinquent installments on them.

We conclude this brief by setting out the language of Judge Cox of the Northern District of New York in the matter of Charles W. Becker:

> "A discharge is intended to relieve misfortune, but it must be misfortune coupled with absolute honesty. It is the reward the law grants to the bankrupt who brings his entire property into court and lays it without reservation at the feet of his creditors. This much the law demands. Where it is evident that he is scheming to be relieved of his debts withholding property which should be applied to their payment, he is not entitled to consideration from the court of bankruptcy. The discharge is denied." (*In Re* Becker, 106 Fed. 54.)

We respectfully contend that this bankrupt is not entitled to the act of grace which he now seeks at the hands of this court. That a bankrupt seeking to avoid payment of his debts, should, in so far as his bankruptcy is concerned, "possess a character above reproach," we believe will be undisputed. This we respectfully submit this bankrupt does not possess. The district judge to whom the Bankruptcy Act gives the right to grant or deny a discharge has so found. (Bankruptcy Act, section 14B.) It is true that the referee to whom this matter was referred for the purpose of taking testimony gave the bankrupt the benefit of the doubt, which we contend is contrary to the spirit of section 14 B 7 of the Act as amended on May 27, 1926. However, the

referee's findings are not conclusive on the district court. The application for discharge must, under section 14 of the Bankruptcy Law and General Order in Bankruptcy No. 12, section 3, be heard and decided by the judge of the court. The referee has no jurisdiction to determine the question, but the court may refer the case to him generally for report. He aids the court like a master in chancery. He can not finally determine the question of discharge or no discharge, but he may be ordered to report the fact and his recommendation or conclusion as to the matter. This is merely to aid the judge, and the court then determines the matter. *In Re Rauchenplat,* 9 A. B. R. 763, unreported in Federal Reporter; *In Re* Grosberger v. B. F. Goodrich Rubber Company, 7 A. B. R. 742, U. S. C. C. A. 3rd Ct.

The discretion of the judge should not be interfered with except in a case amounting to an abuse thereof. Woods v. Little, 143 Fed. 229, 13 A. B. R. 742. U. S. C. C. A., 3rd Ct.

Respectfully submitted,

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